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Supreme Court, U.S.
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No. (1)

IN THE
SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1993

DAVID GREEN, EXECUTOR OF THE ESTATE OF
FREDERICK WILLIAM IRVING LUNDY,

Petitioner

vs.

THE UNITED STATES

Respondent

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

PETITION FOR WRIT OF CERTIORARI

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65 pp

QUESTIONS PRESENTED FOR REVIEW

1. Did the lower court err in failing to enforce Internal Revenue Code (26 USC Sec. 2033) against the IRS despite the plaintiff's possible waiver or failure to timely or properly object to breach of the same by the IRS?

2. Did the lower court contradict all precedent and/or act outside its discretionary power when it a) confirmed the IRS decision that possession to title in real estate automatically confers value and beneficial interest to a taxpayer and
b) determined value of real property in an estate based upon events occurring after the date of death of the decedent?

LIST OF PARTIES TO THE PROCEEDINGS IN THE COURT BELOW

The caption of the case in this Court contains the names of all parties to the proceedings in the lower courts: United States Court of Appeals for the Third Circuit and the Court of Claims.

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A. THE ONLY THING OF VALUE WHICH DECEDENT HAD IN HIS ESTATE AT THE TIME OF HIS DEATH WAS A CLAIM AND THE RIGHT TO LITIGATE ON THAT CLAIM.

B. EVEN THOUGH LOCAL LAW REGARDING OWNERSHIP IS GENERALLY FOLLOWED, IT SHOULD NOT BE FOLLOWED BY THE COURT WHEN THE RESULTS ARE INCONSISTENT WITH THE INTENT OF FEDERAL LAW.

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REFERENCE TO OPINIONS OF COURTS BELOW

No opinion was rendered by the Court of Appeals. See copy of Decision to enter no opinion annexed hereto as Exhibit B.

STATEMENT OF JURISDICTION

JURISDICTION OF COURTS BELOW:

The Petitioner filed suit in the Claims Court pursuant to 26 USC Sec. 7422 seeking a refund of federal estate tax. The Claims Courts jurisdiction was invoked under 28 USC Section 1491. The US Court of Appeals for the Third Circuit then had jurisdiction in this case pursuant to 28 USC Section 1295 (a)(3).

ENTRY OF JUDGEMENT BELOW:

The Court of Claims rendered summary judgment in favor of the Respondent. There was never a trial on the issues or facts of this case. The summary judgment decision was appealed to the Court of Appeals for the Third Circuit who rendered judgment (which judgment was thereafter entered on April 13, 1993 confirming the decision of the Court of

Claims.

JURISDICTION OF THE SUPREME COURT:

The Supreme Court of the United States has jurisdiction to review this case pursuant to Rule 17.1 (c) of the Supreme Court Rules which states that as to Federal Courts of Appeals, it is a ground for certiorari that the Court of Appeals has decided an important question of federal law which has not been, but should be, settled by the Supreme Court.

The federal law which has never been determined by the Supreme Court (nor any other federal court) is whether the IRS has the right to tax "stolen" real property ("stolen" via forged deeds) at its full value in the estate of the victim.

In addition, the Supreme Court of the United States has jurisdiction to review this case pursuant to Rule 17 which permits review

when prevalent case law is not adhered to.

Finally, certiorari is the proper remedy where some right, privilege,or immunity is claimed under federal law, such as question relating to the construction or application of a statute, for example validity of a tax assessment may be question on certiorari.

Hanson v. Denckla (1958), 357 us 235 and Erie R. Co. v Hamilton (1919), 248 US 369.

STATUTE and REGULATION INVOLVED

1. Section 2033 of Title 26 of the United States Code provides that "The value of the gross estate shall include the value of all property to the extent of the interest therein of the decedent at the time of his death."

2. IRS REGULATION RE: 26 USC 2033 - See Appendix D, Section 6.

STATEMENT OF THE CASE

At issue here, is the amount of Estate taxes which the IRS was paid, and if a fraction of such tax should not have been paid. The decedent in this case, Frederick Irving W. Lundy, worked all his life very diligently, starting from a little clam bar in his youth in Sheepshead Bay, New York and developing it into a two thousand seat restaurant which he operated, until his death at the age of 85, in the Sheepshead Bay area of Brooklyn, New York.

Upon his death, the executors reported a gross estate of sixteen million dollars. However, the IRS assessed it at nineteen million dollars, and the Estate paid the IRS a total of ten million dollars in estate taxes plus approximately $150,000 in interest or a total assessment of over ten million dollars.

The main issue between the parties is the different method of valuation of property consisting of twenty-seven parcels of land located in New York State (the "Property"), titles for which, at the time of the decedents death, were no longer in his name. The inheritors, his nieces and nephews, were not aware that the Property had been twice transferred, the second time to a purchaser in good faith and for value, and they filed lawsuits, after his death, to reclaim the Property. During the process, it was discovered that the Property was already transferred twice and was in the name of an unrelated third party.

The first transfer of the Property occurred two months before the decedent's death. The Property was transferred to a corporation named Cruz del Sol, Inc. who in turn transferred the property to two individuals, Wexler and Posner, for alleged consideration of valuable paintings. During the litigation, in a separate criminal

proceeding, two individuals were convicted for fraud in the transfer of the deeds in the first instance; there was no determination of fraud in the transfer of the deeds thereafter. Since there was no determination of fraud upon the second transfer, the Estate settled with the second transferees by paying them $300,000 and accepting from them a twenty-seven Quit Claim Deeds, so that, in effect, the Estate purchased the Property back. The Internal Revenue Service allowed the deduction of $300,000 paid to reclaim the Property but, assessed the Estate for the total value of the Property as if the Property was as saleable as the next because NYS law provides that fraudulent deeds do not transfer title. The IRS then concluded that since title had not transferred, the full value of the Property (less expenses in reacquisition) were to be included in the Estate.

The Internal Revenue Code, 26 USC §2033, provides that only the <u>value</u> of the Property, <u>at the very time of a person's death</u>, should be

assessed for Estate tax purposes (See Appendix D).

The Estate however did not realize any "value" in the "title" to the Property since at the time of decedent's death there had been no determination of fraudulent transfer and a law suit was necessary to quiet title. Thus, all the Estate really had at the time of death was the right to a law suit, a claim, a choice in action. By relying on title as solely determinative of value, the IRS has violated 26 USC §2033 for the following reasons:

1) the IRS failed to focus only on facts known at the time of decedent's death, and at that time there had been no determination of fraud (the claim was settled 2.5 years after the death of decedent when the Estate purchased the Property for $300,000), and

2) the IRS assumed that title gave full value and it is clear that title was obtained only two years later and had no value at time of death. The IRS failed to employ its own beneficial

interest test.

For the foregoing reasons, the beneficiaries, upon realizing that they overpaid the estate taxes, filed a claim for a refund to exclude the Property which was not held in decedent's name at the time of his death. This claim was disallowed by the IRS. The Estate filed a lawsuit with the United States Court of Claims, requesting that the refund be made based on the fact that the Property was not the decedent's to be taxed or in the alternative to include the accounts receivable as a substitution for the land. Such accounts receivable would be the fair market value of the lawsuit.

The Court of Claims had original jurisdiction over this matter pursuant to 28 USC Section 1491. There Court of Claims, noting that there was no dispute as to facts, ruled by summary judgment for the IRS, the Respondents, noting that since title was in the Estate the Estate should be taxed for the Property. The

Court did not address itself to the issue of valuation. The US Court of Appeals for the third Circuit then had jurisdiction to review the appeal of this decision pursuant to 28 USC Section 1295 (a) (3). The US Court of Appeals for the Third Circuit affirmed the decision of the lower court without opinion. See Appendixes A and B.

The Court of Claims ruled that because the forged deed did not transfer the Property, the second transfer which was not forged was also not valid, therefore, the Property, at its full value, less cost of repurchase, remained in the Estate. The Plaintiff, in the oral argument of a summary judgment motion before the Court of Claims, argued that in this case the Property was not saleable and its value still would be worth only as much as the lawsuit. It was then brought to the attention of the lower court Judge, that there is a precedent in the Meador

case[1] where it was ruled that the estate of the thief would be taxed even though the stolen paintings from Germany had been returned to their homeland. The Court of Claims dismissed that precedent, on the ground that paintings were personalty and could be removed, thus possession could be enjoyed, whereas, with "stolen" real property the thief could not enjoy possession. The IRS and the Court of Claims then assumed that possession was full value in itself, without further inquiry into the benefit or value which the possessor could really enjoy eg. the "possessor", the Estate, could not mortgage or sell the Property because title was recorded in another's name, and the Property was vacant land of which a possessor would reap no benefit of possession. In addition, there was no possession by decedent or his Estate as the Property was vacant land. The only real

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[1] Meador v. IRS (IRS ruling decision made Feb. 13, 1992,Index Nos 2031-01-00, 2033-01-00,2053-09-00, Control No. RE-32-259-90

"possession" in this case would be clear record title which did not exist.

The lower courts were silent of the fact that the Property was to remain forever in the new owner's name if the Estate did not commence litigation. Both lower courts failed to acknowledge that. This leaves one to ponder the outcome had the Estate not sought to quiet title by litigation. Who would the IRS then have taxed? If the Estate had not challenged title to the Property, then in that event, the thief would not have been punished and the third party would have full enjoyment of the Property. Would it be likely or even feasible for the IRS then not to tax the thief?

As mentioned before, the third party did sell the Property by tendering the deeds, evidence that ownership was never clear of record. Indeed, as a net result, the Estate would have been better off if it had not challenged the transfer of the Property as the Estate would have saved litigation costs, the

pre-acquisition costs and seventy-five percent taxes on the declared value of the Property.

The Court of Appeals for the Federal Circuit did not take great interest in the substance of the claim, that is, the fact that the IRS never looked to actual value, beneficial interest, which the Estate had in the Property at the time of decedent's death. The Court of Appeals, at the time of oral argument, made it clear that though the value of the Property may have been improperly determined by the IRS, the Petitioner had not timely or properly or often enough stated this concern over valuation but instead focused on title ownership alone, thus the Estate, in effect waived its right to a reduction in taxes based on wrongful valuation despite the valuation standards set forth in 26 USC §2033. The Court of Appeals for the Federal Circuit ignored the fact that the value had been challenged by Petitioner in summary judgment oral argument before the Court of Claims, and less directly in the Petitioner's argument that

the Estate was willing to include the value of the lawsuit to reclaim title to the Property, which in turn would be the value of the Property with all the liens upon it. Indeed, it was only a difference in semantics, completely out of the control of the beneficiaries, on how the attorneys phrased it.

Now the Petitioner comes to the Supreme Court and in substance is asking this Court to correct this inequity and to direct the IRS to comply with the Internal Revenue Code and its own regulations, and therefore, to tax the Property at its value as known at the time of death, title being only one factor of value and not determinative of the issue. The Petitioner seeks an order of this Court directing the IRS to adhere to Internal Revenue Code and regulations which mandate that only "value" be taxed and the an investigation into the value of the Property at the time of decedent's death be made.

This case is a classic example of how the

court process took on a life of its own and was able to get around the intent of the law through collateral issues of estoppel, waiver etc. so as to avoid the enforcement of a statute clear on its face and which statute the IRS does not dispute. If a determination of value is permitted, then Petitioner will have no problem proving that the value of the Property was very little since there was no one willing to buy it or mortgage it, as title of record was in another's name.

By violation of 26 USC §2033, the IRS overreached its powers and authority which is carefully prescribed by law. No waiver can permit a violation of law by a government agency that clearly oversteps its powers and rights. Because of the IRS overreaching to tax the Property as if title conferred full value and based upon facts occurring after decedent's death, the Estate suffered damages in the amount of $807,228 plus costs and attorney's fees, and the Estate was compelled to borrow money and pay

interest to the IRS for not being able to tender cash. Interest was due on top of the seventy-five percent tax assessment. The Estate had to dispose of the Property and give discounts on the mortgages to salvage part of the inheritance.

If the Supreme Court remands this case for a trial to determine the value of the Property in the Estate at the time of decedent's death, the Estate is prepared to show that such value would be substantially lower than that included in the Estate by the IRS.

REASONS FOR GRANTING WRIT

THIS WRIT SHOULD BE GRANTED BECAUSE TO NOT GRANT THIS WRIT WOULD TO PERMIT THE GOVERNMENT TO OVERSTEP ITS TAXING POWER AND VIOLATE DUE PROCESS OF LAW. IN ADDITION, THE HOLDING OF THE COURT OF CLAIMS, AS AFFIRMED BY THE COURT OF APPEALS, CONTRADICTS EXISTING CASE LAW.

A. VALUATION AT TIME OF DEATH

Section 2033 of Title 26 of the United States Code provides that "The value of the gross estate shall include the value of all property to the extent of the interest therein of the decedent at the time of his death."

A. VALUATION AT TIME OF DEATH

In this case the Respondent, by the IRS, failed to focus valuation as of the date of death of the decedent and instead focused valuation based upon subsequent litigation. Focusing on subsequent litigation for valuation and not on valuation at the time of death

breaches the terms of said IRC code and regulations and thus deprives the taxpayer of due process of law guaranteed by Article XIV of the US Constitution and is a violation of the limits of the taxing power of the US Government as set forth in the Constitution.

A recent decision of the Tax Court which was not available at the time this case was presented to the Court of Claims and the Court of Appeals is the decision of the US Tax Court in the Ethlyn Davis case (US Tax Court 28647-90) which was decided May 13, 1993 (see Appendix C). In this case the IRS again attempted to include a full amount of a reward (in this instance 21 million dollars) in an estate, arising from a law suit ruled upon after the decedent's death. The Tax Court did not permit such action by the IRS and reversed the assessment to a market value of the claim as determined at the time of decedents death, and thereby reduced the IRS tax claim to only $46,176. This $46,176 represented the value of the claim as it would be perceived

at the time of decedent's death. The court noted that the actual outcome of the lawsuit was irrelevant because it would not have been known at the time of decedent's death.

B. VALUATION OF STOLEN PROPERTY

In the Meador case,supra,the IRS, through its rulings determined that stolen personalty was to be taxed to the thief's estate even if the stolen property had been returned. The IRS tries to distinguish stolen personalty from stolen real estate stating that with stolen real estate possession is still maintained even though deeds may have been stolen. The courts failed to recognize that the principals of Cruz Del Sol, Inc (the thieves) did obtain possession and sold the property to Wexler and Posner, who then sold it back to the Estate of $300,000. The IRS then took their argument a step further and stated that title never left the estate because a forged deed does not pass title in NYS. The IRS then concluded, that since the

title and possession were both held by the Petitioner, then the full amount of the Property must be included in the Estate less any expenses incurred as a result of any title disputes.

By such reasoning the IRS duped the judge in the Court of Claims who failed to focus on the fact that only "value" as determined by "beneficial interest" can be included in the Estate. The judge below assumed that title and "possession" (remember that the Property is vacant land so possession has little meaning in regards to benefit) meant full value. Normally title and possession would mean full value in the Estate but not in these circumstances. Because the title had been fraudulently transferred, despite NYS law which holds that title does not change by fraudulent deed, a lawsuit would be and was required to quiet title. Thus, all the Estate had at the time of decedent's death was a right to sue, that is, a choose in action.

That title in itself does not impart full

value (less expenses) is set forth in the case of the Estate of Muriel W. Saunders, deceased, Carolyn S. Wendeler, Executrix, v. Commissioner of the Internal Revenue Service, decided September 28, 1989, T.C. Memo 1989-537; 58 TCM (CCH) 282; TC Mem (P-H) 890537. In this case, the court ruled that because there were possessory rights in another, even though title was held by the Estate, the Estate could not be taxed on the property in question, since title alone confers no value. The Tax Court made it very clear that title alone does not confer benefit or value and would not permit a tax were no benefit or value was proven.

Despite the foregoing case, and others like it, due to semantics or no reason at all, the IRS was permitted in this case to consider title as automatic full value.

The Judgment of the Court of Appeals for the Third Circuit should be reviewed by this Court because the Supreme Court's decision in this case would protect the public from

overreaching state agencies which choose to ignore their own regulations when doing so benefits them and would set precedence, where none exists, as to the treatment of "stolen" real estate in a deceased's estate.

CONCLUSION

The IRS may not circumvent its own regulations in the hope that a taxpayer overlooks their wrongdoing or fails to properly or timely raise objection to their wrongdoing.

Even if the lower court was correct in determining that Petitioner did not timely or properly raise the issue of the violation of the valuation standards set forth in 26 IRC 2033, the lower court should have upheld the Code on its face and ordered the IRS to comply with its own regulations.

Thus the important question of law which this court is asked to rule upon is whether a governmental agency can circumvent Federal statute and its own regulations if the unwitting public does not understand or catch the wrongdoing or does not plead well in the court

of first instance.

It would be unconscionable to permit the IRS to issue rulings which see-saw according to how much money they can make. For instance, in the Meador's estate case the IRS declared the property in question to be in the thief's estate. In this case the IRS declares the stolen property to be in the victim's estate.

Likewise, the Tax Court ruling in the Davis case specifically demonstrates that the Estate was assessed on only approximately $46,000, the value of the law suit at the time of the decedent's death. The IRS was not permitted to look at or mention the fact that subsequent litigation established value at 2.1 million, the final reward.

The Supreme Court is a court of last resort and a court of all legal and equitable powers. Thus, only the Supreme Court can correct the obvious injustice that has been rendered in this case.

APPENDIX

A. Judgment of the Court of Appeals, Third Circuit

B. Opinion of The Court of Appeals, Third Circuit.

C. Judgment of the United States Court of Claims

D. Davis Case Report - Summary of Davis Case

E. Opinions and findings of U. S. Tax Court in case of Estate of Ethlyn Davis, deceased, Don M. Davis, Executor, Petitioner, v. Commissioner of Internal Revenue, Respondent

F. Part of Regulation §20.2033-1 and PH Explanation of Section 2033 of the Internal Revenue Code

UNITED STATES COURT OF APPEALS
FOR THE FEDERAL CIRCUIT
92-5118

DAVID GREEN, EXECUTOR OF ESTATE OF
FREDERICK WILLIAM IRVING LUNDY,
Plaintiff-Appellant

v.

THE UNITED STATES,
Defendant-Appellee

JUDGMENT

ON APPEAL from the United States court of federal Claims

in CASE NO(S) 629-86 T

This CAUSE having been considered, it is

ORDERED and ADJUDGED:

PER CURIAM (ARCHER, MICHEL AND RADER, Circuit Judges):

AFFIRMED. Fed. Cir. R. 36

ENTERED BY ORDER OF THE COURT

DATED:_____

_____
Francis X. Gindhart, Clerk

UNITED STATES COURT OF APPEALS
FOR THE FEDERAL CIRCUIT

NOTICE OF ENTRY OF
JUDGMENT WITHOUT OPINION

JUDGMENT ENTERED: APRIL 12, 1993

The judgment of the court in your case was entered today pursuant to Rule 36. This Court affirmed the judgment or decision that was appealed. None of the relief sought in the appeal was granted. No opinion accompanied the judgment. The mandate will be issued in due course.

Costs may be recoverable from the appellant or petitioner in favor of the appellee or respondent under Rule 39. A party entitled to costs is provided with a bill-of-costs form and an instruction sheet with this notice.

The parties are encouraged to stipulate to the costs. A bill of costs will be presumed

correct in the absence of a timely filed objection.

Costs when taxed are payable to the party awarded its costs. If costs are awarded to the government, they should be paid to the Treasurer of the United States. Payment should be made to counsel for the party awarded costs or, if the party is not represented b counsel, to the party pro se. Costs should be paid promptly.

Exhibits and visual aids shall be promptly retrieved by the party that lodged them with this court.

FRANCIS X.

GINDHART, Clerk

GREEN V. US, 92-5118
(CLM - 629-86 T)

UNITED STATES CLAIMS COURT

No. 629-86 T

DAVID GREEN, EXECUTOR OF THE ESTATE OF FREDERICK WILLIAM IRVING LUNDY

JUDGMENT

v.

THE UNITED STATES

Pursuant to the order of March 12, 1992,

IT IS ORDERED AND ADJUDGED this date, pursuant to Rule 58, that the complaint is dismissed. Costs to defendant.

David A. Lampen
Clerk of Court

By:_____
Deputy Clerk

March 13, 1992

NOTE: As to appeal, 60 days from this date, see RUSCC 72, re number of copies and listing of all plaintiffs. Filing fee is $105.

APPENDIX C

APPENDIX D

DAVIS CASE REPORT:

Ethlyn Davis of Huron, S.D. died in 1986 before any trial of her suit accusing Merrill Lynch of fraud in the churning of her securities account. Before her death, the firm offered her $50,000, but the case was tried twice before the firm settled for $2 million. The estate netted $1,065,555 after legal fees and expenses. but for estate tax, the IRS put the taxable value of Davis's claim against Merrill Lynch on the date of her death at $2 million - the sum awarded by a jury after the second trial.

The estate argued in the Tax Court for a value of $62,255. Valuing a lawsuit is an abstract endeavor, Judge Gerber said; he found no basis for the IRS figure. Taking Davis's claim for actual damages of $107,853, the Judge reduced it for costs, delay in recovery,

and a small risk of losing and valued it at $16,176. But he gave no method for valuing potential punitive damages.

"In light of all the evidence, the Judge valued that expectation of $277,056, times the other amount for a date of death value of $323,232.

APPENDIX E

T.C. Memo 1993-155

UNITED STATES TAX COURT

ESTATE OF ETHLYN DAVIS, DECEASED, DON M. DAVIS, EXECUTOR, Petitioner v. COMMISSIONER OF INTERNAL REVENUE, Respondent

Docket No 28647-90 Filed April 8, 1993

Francis m. Smith and Michael M. Billion, for petitioner, J. Anthony Hoefer, for respondent.

MEMORANDUM FINDINGS OF FACT AND OPINION

GERBER, Judge: Respondent, by means of a statutory notice of deficiency, determined a

$678,103 Federal estate tax deficiency. The primary issue concerns the value, for estate tax purposes, of the cause of action against Merrill Lynch, Pierce, Fenner & Smith, Inc. (Merrill Lynch). The litigation involved claims for compensatory and punitive damages in a security churning[1] case. We also consider an evidentiary issue concerning the subject matter of an expert's report and the amount of reliance to be given to it in this case.

FINDINGS OF FACT

Some of the facts have been stipulated, and the stipulation of facts is incorporated

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[1] Churning occurs when an account executive who directs the account's trades initiates transactions that are excessive, for personal gain. Churning can never occur with respect to any transaction directed by the customer.

by this reference. Ethlyn Davis (decedent) died on November 4, 1986, at a time when she resided in Huron, South Dakota. Don M. Davis, the executor of decedent's estate, resided in Florida when the petition in this case was filed.

In 1972, decedent's husband, Leonard Davis, opened an account for decedent with Merrill Lynch, at its Minneapolis office. Mr. Davis died in 1976. Between 1972 and 1981, Edward Marks (Marks), a Merrill Lynch account executive, was responsible for decedent's account. Marks was aware that decedent was an unsophisticated investor and that she completely trusted and relied on the advice of her Merrill Lynch account executives. In May 1981, when decedent was 87 years old, marks transferred decedent's account to a different

account executive, Steven Ulrich (Ulrich). From early 1982 to August 1984, Ulrich churned decedent's account, making between 106 and 141 unauthorized trades. Merrill Lynch earned $43,468 in commissions from the unauthorized trading. During the time the account was being churned, decedent realized a net profit exceeding $53,000. If no trades had been made on decedent's account for the same period, it was contended that the account would have realized over $100,000 of net profit.

On August 21, 1985, decedent brought a suit against Merrill Lynch in the United States District Court for the District of South Dakota. At the time the suit was commenced, Merrill Lynch was a subsidiary of a company with revenues in excess of $9,600,000,000 and a net worth approaching

$2,900,000,000. Decedent's suit alleged that Merrill Lynch had committed fraud and deception in violation of section 10(b) of the Securities Exchange Act of 1934 and rule 10b-5, was guilty of common law fraud and deceit, had breached its fiduciary duty, and had converted decedent's funds to its won use. Decedent sought $122,674.30 in compensatory damages and $6 million in punitive damages. Merrill Lynch defended the action contending that the account was not excessively traded; the law was not clear that there was fiduciary relationship between it and decedent; there were no actual damages because the account increased in value over the period in controversy; and that the law was not clear that punitive damages could be awarded for lack of actual damages, or in Securities

Exchange Act cases, or against a principal for vicarious acts of its agent.

Decedent died on November 4, 1986, and her estate, represented by Don M. Davis, was substituted as plaintiff in the cause of action against Merrill Lynch. When decedent died, the pretrial discovery had not been completed in the Merrill Lynch litigation. The estate tax return (Form 706) was filed February 9, 1988, and listed the Merrill Lynch litigation as a miscellaneous asset with a zero value.

On or about September 23, 1985, Merrill Lynch offered to settle the litigation for $50,000. On April 9, 1987, Merrill Lynch made another offer in the amount of $80,000. Neither offer was accepted and the case proceeded to trial. On May 4, 1987,

decedent's estate received a jury verdict of $20,000 in compensatory damages and $2,250,000 in punitive damages. On July 21, 1987, the District Court ordered decedent's estate to accept a $1,850,000 remittitur (reducing the punitive damages to $400,000) or have another trial only on the issue of damages. The estate rejected the remittitur and there was a second trial. On August 12, 1988, decedent's estate received a second jury award of $100,000 in compensatory damages and $2 million in punitive damages and judgment was entered accordingly. On June 15, 1990, the United States Court of Appeals for the Eight Circuit affirmed the judgment of the District Court. On November 16, 1990, pending appeal to the United States Supreme Court, the District Court approved a $2 million

settlement subject to 45 percent attorney's fees. After fees expenses, decedent's estate received a $1,063,059, which was later adjusted to $1,065,555.

In the notice of deficiency, respondent determined that the date-of-death value of decedent's interest in the lawsuit against Merrill Lynch was $2,100,000. Petitioner contends that the date-of-death value was $62,255.

OPINION

Before considering the valuation issue, we address an evidentiary matter concerning petitioner's expert witness. With the exception of the report and testimony of petitioner's expert witness, the evidence in this case was fully stipulated. The report of Deming Smith (Smith), an expert witness on

behalf of petitioner, was offered at trial. Smith's expertise was acknowledged and his expert witness report was received into evidence over respondent's objections.[2]

Respondent objected to the report on the grounds that Smith had no expertise in churning cases and that his report, in essence, is a brief. Petitioner asserted that Smith, as an experienced trial lawyer, could provide the Court assistance by providing an evaluation method for our use in determining the value of a cause of action for damages.

Rule 702 of the Federal Rules of Evidence provides for the testimony of an expert witness if the expert's specialized knowledge "will assist the trier of fact to understand

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[2] It is noted that respondent did not offer an expert witness in this case.

the evidence or to determine a fact in issue". Smith has practiced as a trial lawyer, specializing in civil litigation in Sioux Falls, South Dakota, since 1946. In that time, Smith has handled and/or evaluated thousands of civil litigation cases. We find that Smith has expertise in evaluating lawsuits. Smith, however has no specialized expertise in the area of securities and churning litigation. Accordingly, Smith's methodology in valuing a lawsuit will be considered in our determination of value. The remainder of Smith's report and testimony will be treated as though it was part of a trial brief or memorandum on behalf of petitioner. On other occasions, the report of a lawyer has been found helpful in determining the value of a cause of action. See Estate of Lennon

v.Commissioner, T.C. Memo. 1991-360; Crossmore v. Commissioner,T.C. Memo 1988-494. We note, however, that expert testimony is received to assist the trier of fact and is not binding to the extent it is found contrary to the court's own judgment. Helvering v.National Grocery Co., 304 U.S. 282, 295 (1938); Estate of Hall v. Commissioner, 92 T.C. 312, 338 (1989).

For Federal estate tax purposes, the value of the gross estate is determined by including the value at the time of death of all property in which decedent had an interest, real or personal, tangible or intangible. Sec. 2031(a), 2033.[3] The value

[3] All section references are to the Internal Revenue Code as in effect at the date of decedent's death, and all Rules referenced are to the Tax Court Rules of Practice and Procedure, unless otherwise indicated.

of the property is the fair market value on the date of death. Fair market value is defined as "the price at which the property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or to sell and both having reasonable knowledge of relevant facts." Sec. 20.2031-1(b), Estate Tax Regs.; United States v. Cartwright, 411 U.S. 546, 5551 (1973).

Valuation is based on facts reasonably known at the date of valuation. This Court has adopted the rule that "subsequent events are not considered in fixing fair market value, except to the extent that they were reasonably foreseeable at the date of valuation." Estate of Gilford v. Commissioner, 88 T.C. 38, 52 (1987).

Having set forth these rather familiar

principles for determining fair market value, we must admit that the valuation of a lawsuit continues to be a unique and abstract endeavor. A lawsuit is not the type of asset, either tangible or intangible, which readily fits within the categories of things regularly traded in commerce. Furthermore, the valuation process for lawsuits does not appear to be as objectively achievable as other types of assets. The concepts underlying law suits for punitive damages make valuation questions even more elusive and difficult to ascertain with a high degree of certainty.

Respondent's determination that the value of the lawsuit was $2,100,000 seems to be derived from the amount of the judgment affirmed by the Court of Appeals, almost 4 years after decedent's death. In reaching

that determination, it appears that respondent did not reduce the value by the amount of legal fees and expenses, which must necessarily be considered. Respondent has provided no rationale for the contention that $2,100,000 is the value. The amount of recovery subsequent to the date of death does not to control the value of the cause of action. American National Bank &Trust Co. v.Commissioner, 594 F. 2d 1141, 1144-1145 (7th Cir. 1979); Estate of Biagioni v. Commissioner, T.C. Memo. 1981-660

Petitioner's expert's (Smith) methodology began with the amount of the claim as if there were no contest and then discounted it for; 1)Costs of litigation 2) hazards of litigation, and 3) time delay in receiving

funds.[4] This same type of methodology was utilized and met with approval in Estate of Cobb v. Commissioner, T.C. Memo. 1982-571. We believe that this approach is an acceptable method to value the portion of decedent's cause of action for compensatory damages.

The amount of the claim for compensatory damages set forth in the complaint was $122,674.30. This was the amount of the claim if there were no contest. We first adjust this amount to reflect the amount of actual damages, because if there was a contest, the damage claim would be automatically reduced to reflect actual damages. Smith determined this

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[4] The order in which the discounts are applied will have some effect upon the final value determined. Although Mr. Smith's order of discounts fits within the pattern of his methodology, we note that it does not represent the only possible approach or order that could have been used.

amount to be $107,863. The $107,853 was derived as follows:

Value of account if no churning had occurred
$211,976
Value of account after churning
156,341
Difference
55,635
Money added to account by decedent
16,750
Churning commissions charged against account
43,468
Amount repaid by broker
(8,000)

Total Compensatory claim for damages
107,853

We note that respondent did not specifically dispute Smith's computation or method, but instead argued that his entire report was a brief. In some respects, we find Smith's preliminary compensatory damage analysis to be persuasive. Accordingly, we accept the $107,853 amount as the first

adjustment in the compensatory damage claim analysis. Next, we reduce that amount for costs of litigation. The legal fees were figured at one-third, which after 6 percent sales tax would be about 35.3 percent. Auditing estimated trial expenses, we arrive at a 45 percent discount. Accordingly, after taking into account attorney's fees and costs of litigation, the compensatory damage claim would be reduced to $59,319; i.e., $107,853 x (1 - 45%).

Based upon the relative ease in proving the churning, our analysis of South Dakota precedent, and the acute nature of the facts, there were only negligible risks or hazards of success in litigating the compensatory damage claim. We also note that Merrill Lynch offered to settle for $50,000 and then for

$80,000 prior to trail. Those offers likely reflect a recognition that compensatory damages were a near certainty,but reflect little, if any, acknowledgement of the potential for punitive damages. Accordingly, we use a 5 percent risk factor in connection with the litigating hazards of the compensatory damage claim. Therefore, we further reduce the value to account for the risk to$56,353; i.e. $59,319 x (1- 5%). Additionally, we discount potential recovery for time delay. Smith used a 2 year delay factor at a 10 percent discount rate to account for the time delay. We also discount the amount for 2 years at a 10 percent discount rate in reaching the fair market value of $46,176 for the compensatory portion of the decedent's claim.

Punitive damages, unlike the compensatory damages, are awarded in connection with the defendant's culpable state of mind. The culpability is usually founded on acts which are malicious, oppressive, wanton, or fraudulent, or involve conscious disregard for the rights of others. S.D. Codified Laws Ann. Sec. 21-3-2 (Michie 1987).[5] Moreover, the purpose of punitive damages is to punish and deter the defendant and like-minded persons

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[5] S.D. Codified Laws Ann. Sec. 21-3-2 (Michie 1987) contains the following:

In any action for the breach of an obligation not arising from contract, where the defendant has been guilty of oppression, fraud, or malice, actual or presumed, or in any case of wrongful injury to animals, being subjects of property, committed intentional or by willful and wanton misconduct, in disregard of humanity, the jury, in addition to the actual damage, may give damages for the sake of example, and by way of punishing the defendant.

from committing similar acts in the future.[6] Because the main purpose is not to compensate the plaintiff or injured party, our analysis follows a different approach than we used for compensatory damages.

First, we note that a plaintiff has no right to punitive damages. This is so even if the defendant acted with a culpable state of mind.[7] The amount of punitive damages is completely discretionary and the finder of fact can take into account the purpose(s) of the award, including the extent of injury, the wealth of the defendant, the plaintiff's litigation expenses, the probability of repetition of the conduct, etc.

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[6] Schlueter & Redden, Punitive Damages, secs. 1.3(E), 2.2 (2d ed. 1989).

[7] Id. sec. 2.1 (C).

In South Dakota, punitive damages are not allowed without the prerequisite of a compensatory damage award. Speck v. Anderson, 349 N.W. 2d 49, 51 (S.D. 1984); Johnson v. Kirkwood, Inc., 306.N.W. 2d 640, 643 (S.D. 1981). At the times of decedent's claim, lawsuit, and death, the courts of South Dakota had not yet considered; 1) Whether there was a fiduciary relationship between a stockbroker and client, and 2) whether a principal (Merrill Lynch) could be vicariously liable for punitive damages awarded in connection with the acts of its agent.[8]

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[8] At the time of decedent's death the Supreme Court of South Dakota had upheld punitive damages in the following multiples:

Punitive Damages	Compensatory Damages	Multiple
$6,600	$2,200.00	3.0
100,000	244,922.99	.4
50,000	4,574.46	10.9
20,000	3,177.84	6.3

These concepts, however, may not have meaningful relevance to the hazards in pursing

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7,000	200.00	35.0

Smith's report also contained a list of six cases decided by Federal Courts of Appeals involving churning where plaintiffs were successful in obtaining punitive damages against the stock brokerage companies, as follows:

Punitive Damages	Compensatory Damages	Multiple
300,000	46,675	6.4
1,500,000	175,000	8.6
200,000	37,000	5.4
100,000	54,000	1.8
16,000	30,000	0.5
66,666	24,600	2.7

We note that neither party provided referenced for South Dakota churning cases other than the one being valued. Additionally, we accepted petitioner's expert's case references for punitive damages in South Dakota and punitive damages in churning cases in Federal Courts of Appeals. Respondent did not disagree with these citations or provide additional references from which other or contradictory conclusions could be drawn.

punitive damages because no information was provided regarding unsuccessful punitive damage litigation in South Dakota or churning litigation in Federal courts. Moreover, there does not appear to be any generally established principle that punitive damages bear any direct numerical relationship to compensatory damages.

With these impediments in mind and recognizing the paucity of information available we slide down this slippery slope to the point where we grasp the maxim that "Valuation for estate tax purposes frequently involves difficult and somewhat imprecise calculations." Estate of Biagioni v. Commissioner, T.C. Memo 1981-660 (citing Estate of SMith V. Commissioner, 57 T.C. 650 (1972), affd. 510 F.2d 479 (2nd Cir. 1975)).

Based upon the facts, case precedent, and accounting for attorney's fees and costs of litigation, we find the fair market value of decedent's claim for punitive damages was $277,056 as of the date of death.

Therefore, in light of all the evidence presented, we find that the fair market value, as of the date of death, of decedent's cause of action against Merrill Lynch was $323,232 ($46,176 compensatory damages and $277,056 punitive damages).

Decision will be entered under Rule 155.

UNITED STATES TAX COURT

Washington, D.C.

CERTIFICATE

I, CHARLES S. CASAZZA, Clerk of the United States Ta court, do hereby certify that the document(s) attached hereto is a true copy of MEMORANDUM FINDING OF FACT AND OPINION (T.C. Memo, 1993-155) filed April 8, 1993 filed in the case of ESTATE OF ETHLYN DAVIS, DECEASED, DON M. DAVIS, EXECUTOR, Petitioner v. COMMISSIONER OF INTERNAL REVENUE, Respondent.

Docket No. 28647-90 in this Court, and that the original documents in that case are in my official custody and are on file in my office.

IN TESTIMONY WHEREOF, my signature and the seal of the Court are affixed hereto at Washington, DC, this 13th day of May, 1993.

CHARLES S. CASAZZA
Clerk of the Court

REGULATION §20.2033-1 AND
PH EXPLANATION OF SECTION 2033 OF THE INTERNAL REVENUE CODE

REGULATION §20.2033-1

Internal Revenue Code Regulation §20.2033-1 (TD 6296, filed 6-23-58; amended by TD 6684, filed 10-23-63). Property in which the decedent had an interest (a) In general. The gross estate of a decedent who was a citizen or resident of the United States at the time of his death includes under section 2033 the value of all property, whether real or personal, tangible or intangible, wherever situated beneficially owned by the decedent at the time of his death....

PH EXPLANATION OF SECTION 2033 OF THE INTERNAL REVENUE CODE

120,330: Sec. 2033 [120,331] includes in the gross estate the value of ownership is a vital factor in determining its tax status under this section. Generally, local property law controls the issue of ownership for tax purposes.

However, in U.S. v. Chandler, the U.S. Supreme Court said that the Federal regulations may pre-empt inconsistent state property law, as in the determining the effectiveness of transfer of jointly held U.S. Series E Bonds. In Comm. v. Bosch's Est., the U.S. Supreme Court said that a Federal court is conclusively bound by a State court's adjudication of what the property rights under state law are only if it is the highest court of the State. See 120,334.

CERTIFICATE OF SERVICE

I hereby certify that on June 11, 1994, triplicate true and correct copies of the annexed Petition for Writ of Certiorari with required supporting papers were served by overnight mail (Federal Express) to Respondent's attorney in triplicate at upon:

G. Robson Stewart
Tax Division
Dept. of Justice
10th and Constitution NW
Room 4324
Washington, D.C. 20530

with an additional copy sent to:
Solicitor General
Department of Justice
Washington, D.C. 20530

Date: June 10, 1994

Victoria M. Brown

Victoria M. Brown, Esq.